**Alaska Telephone Association**
4341 B Street, Suite 304
Anchorage, AK 99503
(907)563-4000
FAX (907)562-3776

Duane C. Durand
President

James Rowe
Executive Director

May 16, 1996

William F. Caton
Acting Secretary
Federal Communications Commission
1919 M Street, N.W.
Room 222
Washington, D.C. 20554

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF SECRETARY

RE: CC Docket No. 96-98

Dear Mr. Caton:

The Commission's decisions regarding the issues in this docket are vital to our customers and system of telecommunications in Alaska.

Thank you for your attention.



Very Truly Yours,

James Rowe

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF SECRETARY

BEFORE THE
FEDERAL COMMUNICATIONS COMMISSION
WASHINGTON, D.C. 20554

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|---|---|---|
| In the Matter of | ) | |
| | ) | CC Docket No. 96-98 |
| Implementation of the Local Competition | ) | |
| Provisions in the Telecommunications Act | ) | |
| of 1996 | ) | |

**COMMENTS OF THE ALASKA TELEPHONE ASSOCIATION**

The Alaska Telephone Association ("ATA"), a trade association representing twenty-two local exchange companies in Alaska, provides herein comments in the above referenced proceeding.

ATA focuses its comments on what it believes are fundamental issues to this proceeding. These issues are: One, the authority and responsibilities of the Federal and State Commission to implement the Telecommunications Act of 1996 and the incumbent Local Exchange Carrier's ("LEC") role in good faith negotiations. Two, the incumbent LEC's need to rebalance rates in light of a new competitive market. Three, the appropriate costs incumbent LECs are allowed to recover so that the spirit of the Telecommunications Act is achieved. ATA will also provide comments concerning Exemptions, Suspensions and Modifications.

## The Authority and Responsibilities of the Federal and State Commission and the Role of the Incumbent LEC

ATA believes it is not necessary for the Federal Commission to attempt to promulgate "specific" methods for the development of rates for Interconnection, Collocation, Unbundled Rate Elements and Resale obligations of the LEC. Instead, the Commission should set broad and flexible guidelines to insure that competitive entry to the LEC market will take place in a consistent manner while maintaining the goals of Universal Service. Throughout the Commission's Notice of Proposed Rule Making ("NPRM") the Commission proposes specific guidelines and regulations regarding interconnection and unbundling. ATA urges the Commission to avoid heading in this direction for the following reasons: First, the Congress of the United States specifically empowered the State Commissions to set just and reasonable rates for Interconnection, Collocation, Unbundling, and Resale[1]. Even the States' involvement in setting rates is limited to resolving disputes that may arise and consummating agreements after determining that rates are just and reasonable. Second, Congress provided preemption authority to the Federal Commission in the event that a State Commission fails to perform the duties required by the Act. Congress would not have provided preemption authority[2] if it did not intend a primary role for the State.

ATA believes the Telecommunications Act is clear in the role and responsibilities of all parties. First, the incumbent LEC and new entrant meet in good faith negotiations to reach

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1 See the Telecommunications Act of 1996, Section 252(d) "PROCEDURES FOR NEGOTIATION, ARBITRATION, AND APPROVAL OF AGREEMENTS - PRICING STANDARDS" For Interconnection and Network Element Charges, Charges for Transport and Termination of Traffic, and Wholesale Prices for Telecommunications Services.

2 The Telecommunications Act of 1996, Section 253(d) "PREEMPTION" empowers the Federal Commission, "If...the Commission determines that a State or local Government has permitted or imposed any statute, regulation, or legal requirement that violates subsection (a) or (b), the Commission shall preempt the enforcement of such statute...to correct such violation or inconsistency."

agreement; second, the State is empowered to approve the rates upon determination that the rates agreed upon are just and reasonable, and if necessary, resolve any disputes between the parties; and finally, if the State fails to act, the Federal Commission assumes the responsibility of the State Commission.

The Act specifically details that the States have the primary role in overseeing interconnection agreements. The FCC should provide general guidelines for compliance with the Act. These guidelines for pricing unbundled services should address the implicit subsidies and rate averaging built into current local rate structures and regulations to ensure competitive neutrality.

## Incumbent LECs Will Need To Rebalance Rates

Incumbent LECs have to rebalance rates in light of the new competitive market. In accordance with Universal Service goals, LECs have traditionally set rates based upon the provision of service to all customers at affordable rates. As a result, basic services may be priced below cost. If LECs are not allowed to rebalance their rates based upon a new competitive market place, high contribution services will be at risk. As LECs lose these high contribution services there will be increased pressure on basic services, thereby putting them also at risk.

Additionally, most LECs will need to rebalance their rates to reflect shorter useful depreciable life of their assets. This is true for two reasons: First, LECs have traditionally kept rates low by extending the depreciable life of their assets beyond its useful life. Two, the depreciable life of an asset changes when both competition and technology come into play. Telecommunications technology is evolving at a pace where equipment can be replaced with better and less expensive equipment prior to the expiration of its depreciable life. In an aggressive, competitive market place, competition will limit the useful life of an asset by finding alternative ways of providing service through packaging or other marketing strategies. Therefore, the LEC would be at a competitive disadvantage if it were forced to develop its costs absent its ability to rebalance its rates.

## Appropriate Costs LECs Should Recover In Interconnection Rates

In its NPRM, the Commission seeks comment on the appropriate incremental cost, (Long Run Incremental Cost "LRIC" or Total Service Long Run Incremental Cost ("TSLRIC") methodology that should be used to set rates charged to the new entrant wishing to interconnect to the incumbent LEC's network.

ATA believes incremental cost is an inappropriate tool to develop interconnection rates for the following reasons: First, incremental costs have historically been used as a cost floor to insure that LECs do not attempt to cross subsidize competitive services on the backs of its basic service offerings. Second, interconnection rates can not be set at incremental costs because they do not recover the embedded cost of the incumbent LEC, and therefore would be confiscatory. Third, incremental costs would not achieve the goals intended in the Telecommunications Act of 1996.

Concerning the first point, to avoid cross subsidization fears by the Commission, incremental costs have been used as a cost floor, rather than a price ceiling as suggested within this NPRM. In fact, the Commission typically required that a return component be included in addition to the cost so that some contribution would be made to the LEC's joint and common costs. The rationale behind this methodology was that the LEC was economically better off by obtaining some contribution to offset basic service rates rather than losing the customer. However, this economic theory fails in a competitive market because the LEC, by offering its competitor rates at incremental cost, actually loses market share and its associated contribution!

Regarding point two above, incremental cost must include the embedded cost of the incumbent LEC network. The failure to include these costs in the rates charged for interconnection results in either burdening other LEC services, causing them to be further susceptible to competition, or be left unrecoverable.

In addition, using LRIC costing is not in the spirit of the Telecommunications Act. The Act envisioned that customers would have more choice, and that choice means that more than one provider and network is available. However, if LECs are not allowed to recover their true embedded cost to provide interconnection, new entrants will not have any motivation to develop their own facilities.

An incumbent LEC is at a competitive disadvantage when it must provide both wholesale rates and interconnection to the same entrant. The new entrant could game the system by alternately choosing to interconnect or accepting the incumbent's wholesale tariff. Attachment #1 provides an example illustrating this point. As shown in Attachment 1, the new entrant will build facilities where it is cheaper than paying the incumbent's rate (customer category D and E). Conversely, the new entrant will purchase from the incumbent LEC where it is cheaper than building facilities (customer category A, B, and C), even at the incumbent's retail rates! Such tariff shopping results in an average cost per line for the new entrant to be materially less than the incumbent and, therefore, does not meet the "competitive neutrality" required by the Telecommunications Act of 1996. The Commission should recognize that the system is flawed when customers are permitted to mix and match the incumbent LEC's wholesale tariffs and interconnection agreements. ATA recommends that the Commission should allow new entrants the option of either purchasing from the LEC's wholesale tariff or negotiate an interconnection, but not be able to shop both the wholesale tariff and have interconnection.

## Exemptions, Suspensions, and Modifications

The Commission seeks comment on whether it can and should establish some standards that would assist the states in satisfying their obligations under Section 251(f), "EXEMPTIONS, SUSPENSIONS AND MODIFICATIONS." ATA has reviewed the initial comments of the United States Telephone Association ("USTA") and concurs that the Commission should establish basic guidelines for bona fide requests.

Section 251(f)(2) is the result of three years of careful deliberation and debate in the Congress. Therefore, the Commission should ignore any misrepresentations by anyone who, through public relation blitzes or by any other means, attempts to portray this section as a "loop hole" to qualified incumbent LECs when the record laying the intended purpose of this section of the Act has existed for years. In addition, smaller rural incumbent LECs have specific exemptions within the Act that recognize their own unique market characteristics to insure a level playing field. Section 251(f)(2) is the regulation that protects the public interest, convenience, and necessity insuring that the State can provide oversight to fair and competitive entry.

## Summary

Both the Federal and State Commissions have important responsibilities in implementing the Telecommunications Act of 1996. The Federal Commission can, and should, set broad and flexible policies that insure a level playing field consistent with universal service requirements and leave to the State the responsibility of developing specific interconnection regulations. The incumbent LEC must be able to prepare itself for competition by rebalancing its rates in advance of offering services to the new entrant. The Federal Commission should not impose costing methodologies on the incumbent LEC to set rates for the new entrants. Interconnection, collocation, unbundled, and resale rates should be arrived at through good faith negotiations and approved by the State pursuant to the guidelines outlined in the Telecommunications Act. Finally, LRIC costing is an inappropriate tool to set price because it does not recover the embedded costs of the incumbent LEC and would not result in the development of advanced networks

Respectfully submitted this 16th day of May 1996.

James Rowe
Executive Director
Alaska Telephone Association
4341 B Street, Suite 304
Anchorage, AK 99503
907/563-4000 FAX 907/562-3776

## Incumbent LEC Cost Structure

| Customer Category Based On Cost per Line | Monthly Cost per Subscriber | # of Subscribers | Total Monthly Cost | Retail Rate/Mo. 20 | Total Monthly Revenue | Profit <Loss> Generated |
|---|---|---|---|---|---|---|
| A | 100 | 5 | 500 | 20 | 100 | (400) |
| B | 50 | 10 | 500 | 20 | 200 | (300) |
| C | 20 | 15 | 300 | 20 | 300 | 0 |
| D | 10 | 30 | 300 | 20 | 600 | 300 |
| E | 5 | 40 | 200 | 20 | 800 | 600 |
| | | 100 | 1800 | | 2000 | 200 |

Average Cost per line $18.00

**New Entrant's Cost Structure**

A new entrant can build facilities where it is cheaper than paying the incumbent's rate. The new entrant will purchase from the LEC where it is cheaper than building facilities, even at retail rates.

If the new entrant can build facilities for no more than the "inefficient, high cost, monopoly LEC," the new competitor's WORST CASE cost and price structure would be:

| Customer Category Based On Cost per Line | Monthly Cost per Subscriber | Total # of Subscribers | Retail Monthly Cost | Rate/Mo. 20 | Total Monthly Revenue | Profit <Loss> Generated |
|---|---|---|---|---|---|---|
| A | 20 | 5 | 100 | 13 | 65 | (35) |
| B | 20 | 10 | 200 | 13 | 130 | (70) |
| C | 20 | 15 | 300 | 13 | 195 | (105) |
| D | 10 | 30 | 300 | 13 | 390 | 90 |
| E | 5 | 40 | 200 | 13 | 520 | 320 |
| | | 100 | 1100 | | 1300 | 200 |

Average Cost per line $11.00

This demonstrates that the new entrant will have an unbeatable competitive advantage unless the new entrant is forced to pay the subsidy for carrier-of-last-resort service currently provided from categories D & E to A, B, & C under the incumbent LEC's pricing structure.

This is not the "competitive neutrality" required by the 1996 Act.